United States Court of Appeals

for the Second Circuit

APPELLEE'S REPLY BRIEF

75-6011

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

No. 75-6011

UNITED STATES OF AMERICA,
Plaintiff-Appellant,

vs.

HEALTHCO, INC.,
Defendant-Appellee.

ON CROSS-APPEALS FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

REPLY BRIEF FOR HEALTHCO, INC.

EDWARD L. FOOTE
THOMAS WM. BIANCHI
Attorneys
WINSTON & STRAWN
Suite 5000
One First National Plaza
Chicago, Illinois 60603

Of Counsel:

IRA M. MILLSTEIN
PETER D. STANDISH
Attorneys,
WEIL, GOTSHAL & MANGES
767 Fifth Avenue
New York, New York 10022

INDEX

LIST OF AUTHORITIES

CASES

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

No. 75-6011

UNITED STATES OF AMERICA,
Plaintiff-Appellant,

vs.

HEALTHCO, INC.,
Defendant-Appellee.

ON CROSS-APPEALS FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

REPLY BRIEF FOR HEALTHCO, INC.

I

Introduction

This appeal challenges the District Court's finding that the government has proven a violation of Section 7 of the Clayton Act based upon Healthco's acquisitions in the "dental equipment" market.

Healthco asserts that the government failed properly to measure the size and scope of the relevant market, which the courts have consistently held is the government's burden. *United States* v. *Brown Shoe Co.*, 179 F. Supp. 721 (D.Mo. 1959), *aff'd.*, 370 U.S. 294 (1962); see also *United States* v. *Aluminum Company of America*, 377 U.S.

271 (1964). As a result the Court below improperly relied upon an incomplete government market survey and improperly ignored significant and substantial categories of dental equipment sellers. In addition, the Court below did not recognize that the dental equipment market is a dynamic, growing, and highly competitive market, and has become more competitive since the time of the acquisitions in question. This failure directly conflicts with the Supreme Court's decision in *United States* v. *General Dynamics Corp.*, 415 U.S. 486 (1974), requiring a recognition and analysis of the dynamic nature of competition in the market involved.

The government's Reply Brief misstates Healthco's position by claiming that Healthco seeks to undermine the District Court's decision and to create a different relevant market. That is not Healthco's contention. The Court below found a violation in the relevant product market of dental equipment sales. Healthco does not dispute that dental equipment sales are a relevant product market. However, Healthco believes that the Court erred—given its own market definition—by failing to include as part of that market sales of such products by all competing dental equipment sellers. As a result, the Court below found market shares which do not coincide with competitive realities, and which grossly overstate Healthco's competitive posture in the market.

Contrary to the thrust of the government Reply Brief, the Court below did *not* find that sales of dental equipment by one type of seller, the local dental dealer, comprised a separate line of commerce. Nor has the government adduced any evidence which would demonstrate anything sufficiently different about the various categories of dental equipment purchasers (*i.e.*, dental laboratories, institutions, governmental agencies and dentists) which prevents them

from buying from all types of sellers: dental dealers, manufacturers, and mail order dealers.*

The government did convince the District Court that *new* dentists probably need a local dental dealer to help them set up their practice. The Court below, however, did not find that sales by local dental dealers to new dentists constitute a separate submarket. In fact, the government specifically disclaims such a position.** However, the Court below appears to have used this conclusion regarding sales to new dentists to totally ignore the broad competitive impact of manufacturers and mail order dealers in selling to established dentists, laboratories, institutions and government agencies, and erred by holding that such sales need not be included to determine the size of the relevant market. Sales to these purchasers represent the vast majority of dental equipment sales. Hence, suppliers of such purchasers can not properly be excluded from the market.

Dental dealers, including Healthco, face substantial competition, including competition in the sale of equipment, from at least six categories of sellers, either ignored or not properly considered by the District Court and the government. In its Reply Brief, the government appears willing to include one portion of manufacturer sales previously excluded by the District Court, but still ignores six categories of sellers, as discussed below. The proper inclusion of such manufacturer sales, and the sales of the six addi-

* The government apparently does not dispute the existence of competition among dental dealers, manufacturers and mail order dealers in selling to laboratories, institutions or governmental agencies. It has concentrated only upon issues involving the sale of dental equipment to dentists, notwithstanding the fact that such sales have not been defined to comprise a relevant market and the fact that the record would not permit a calculation of the share of total equipment sales to dentists.

** The government Reply Brief, in mischaracterizing Healthco's argument, recognizes with respect to submarkets such as new dentists, that such submarkets "probably would not qualify as relevant markets." (Government Reply Brief 7, hereinafter "GRB ".).

tional categories of sellers, demonstrates that the government failed to meet its burden of properly measuring the size of the relevant market. As a result, the Court below has vastly understated the size of the relevant market, and thereby mischaracterized Healthco's position in the market.

The proper inclusion of all competing sellers also demonstrates that competition in the sale of dental equipment bears most of the same functional characteristics which the District Court found dispositive in ruling that no anticompetitive effects could be found in the dental sundries market. Specifically, as discussed below, a proper view of the market demonstrates (in addition to a much lower market share for Healthco): (1) the lack of concentration in the dental equipment market, (2) the presence of growing competition in that market, (3) the existence of new entrants in the Metropolitan New York area, (4) the lack of any substantial barriers to enter into the dental equipment market, (5) the existence of additional price competition, and (6) the presence of new and increasing numbers of manufacturers supplying dental equipment to sellers in the market. All of these facts, and particularly the changing nature of competition in the market and the entry of new competitors, must lead to the proper conclusion that competition in the sale of dental equipment to dentists, institutions, laboratories and government agencies has increased, not decreased, since the acquisitions, and that no violation of Section 7 existed.

I

The Government's Reply Brief Begins to Recognize the Broader Scope of Actual Competition, but Ignores Six Categories of Competitors in the Sale of Dental Equipment.

The essential dispute on appeal involves the basic question of whether all competition in the sale of dental equipment to dentists was considered by the District Court.* The District Court concluded, without support of record evidence, that (i) manufacturers were not substantial competitors of dental dealers for relevant sales to dentists; and (ii) mail order dealers accounted for an insignificant amount of relevant sales to dentists. On this assumption, and ignoring these sources of supply, the Court below relied upon the government's market share evidence and found a violation of Section 7.

The basic defects in the government survey from which its market share evidence was created is that the government surveyed only one segment of the relevant dental equipment market—sales by certain local dental dealers. The government has the burden of proof in a Section 7 case to define a relevant market and to present evidence of the size of that market by including all relevant categories of sales in the market. *United States* v. *Brown Shoe Co.*, 179 F.Supp. 721 (D.Mo. 1959), *aff'd.*, 370 U.S. 294 (1962); *United States* v. *Bethlehem Steel Corp.*, 157 F. Supp. 877 (S.D.N.Y. 1958); see also *United States* v. *Aluminium Company of America*, 377 U.S. 271 (1964). The government's limited, gerrymandered view of competition is contrary to the evidence, and fails to meet its burden of proof.

* The District Court did not suggest any absence of competition among dental dealers, mail order dealers and manufacturers in the sale of dental equipment to customers other than dentists, and the government has not disputed this conclusion.

The government has begun to recognize, at least partially, that other categories of competitors should properly be included in the market. Thus, the government has partially revised its market definition by including certain manufacturer sales in attempting to anticipate that this Court may find that "the district court has erred in excluding manufacturer sales." (GRB 10-12). In addition, the government has invited this Court to reconstruct the market share figures downward "if it so chooses." (GRB 13).

The government's position (although couched in terms that even if these additional sales are included the result should not change) is reflected in its statement as to how the scope of a competitive market should be measured:

> ". . . we believe that markets which include sales to all classes of customers are relevant markets for purposes of analyzing the effects of this combination of dental dealers. The companies which Healthco acquired sold their products to all classes of customers." (GRB 6a).

Healthco agrees that any proper analysis from the *purchaser* side of the market must include all classes of customers. However, it is equally true, and the government must also recognize, that the *supply* market must include all classes of competing *suppliers,* not just the local dental dealers the government surveyed, to determine the relevant market. The government cannot ask this Court on appeal to revise the findings below by only including some of the competing sales, while still ignoring the other categories of sellers in the market. The government has pointedly ignored the fact of existing additional competition, asking the Court to use only the limited sales data it developed. This limited approach is analogous to attempting to define the nature of competition in selling women's clothing to the consumer by using only sales figures for department stores, but ignoring the fact that consumers also purchase from dress shops,

discount stores, mail order catalogs, manufacturers' outlets, etc. That type of approach was specifically rejected in *United States* v. *Gimbel Bros., Inc.*, 202 F. Supp. 779 (D. Wisc. 1962), where the court found that "the relevant product market is comprised of much more than that of department stores alleged by the plaintiff . . . there are literally hundreds of effective competitors of department stores, many of which share varying degrees of what the plaintiff claims are the 'unique characteristics' of defendants." (*Id.* at 780) See also *The Papercraft Corp.*, 78 F.T.C. 1352, 1418-1420 (1971).

The government also failed to meet its burden of proving the size of the relevant market in *United States* v. *Columbia Pictures Corp.*, 189 F. Supp. 153 (S.D.N.Y. 1960), where the court concluded that the government's proof was insufficient since it offered evidence only of a portion of the line of commerce, ignoring the competitive realities of the industry. It had obtained no evidence on sales in the actual range of competition which existed.

In *International Telephone & Telegraph Corp.* v. *General Telephone & Electronics Corp.*, 1975-1 CCH Trade Cas. ¶ 60,291 (9th Cir. 1975), the Ninth Circuit rejected a market share analysis finding "no rational basis" to exclude from the relevant market categories of sales which involved the sale of products purchased at comparable prices. The plaintiff had shown no basis for excluding such sales and so the Court concluded that "there are no corresponding factors of competitive significance such as differentiation of product lines, production facilities or pricing" to justify excluding those sales. *Id.* at 66,151.

Similarly the Supreme Court has recognized that the definition of a relevant market of sellers must reflect competitive realities and not be limited to only a portion of the actual competitors of the market. *United States* v. *Continental Can Co.*, 378 U.S. 441 (1964). There, the Court

included glass and metal containers in the relevant market, even though there were obvious differences in the products, and even though some customers preferred one type of supplier over the other at various times. The Court did so because there was in fact competition between glass and metal container suppliers and because both represented alternate sources of supply to container purchasers.

In order to provide a true competitive picture of the dental equipment market, found by the Court below, all sources of supply to dental equipment purchasers should have been included in the government's analysis.

These sources of supply (other than those manufacturers which the government now appears willing to concede can be included), are described below:

1. *Manufacturers Other Than Those Surveyed.* The government makes no representation that the manufacturers it is now willing to include constitute all manufacturers of dental equipment selling in the New York area. The facts indicate that there are an enormous number of others which have not been included and that the government survey may have included as few as 10% of such manufacturers. (JA 321e-JA 324e; JA 438a-JA 439a; JA 165e-JA 179e)

2. *New Manufacturers.* Subsequent to the time periods included in the government's partial survey of manufacturers, many new manufacturers of dental equipment have entered the market and represent sources of supply to the various buyers of equipment. Since 1969, at least 11 dental chair manufacturers have entered the markets; at least 26 dental unit manufacturers have entered the market; and more than 25 other manufacturers of smaller dental equipment have entered the market. (JA 875a-JA 859a). These new manufacturers also provide a wide variety of new sources of supply for new dental dealers, for existing dental dealers entering into equipment sales, and for mail order dealers.

3. *Dental Dealers Outside Metropolitan New York.* If, as the government contends, competition exists between dental dealers as far north as Rockland County in upstate New York and dental dealers in Suffolk County on Long Island, it is obvious that dental dealers in Connecticut, other portions of upstate New York, the balance of New Jersey, and eastern Pennsylvania must also provide competition to dental dealers in Metropolitan New York. The government has failed to survey those dealers or to establish their competitive impact in selling in the Metropolitan New York area.

4. *Metropolitan New York Dental Dealers Not Surveyed.* The government, although stating at one point in its Reply Brief that it "contacted every seller of dental products in Metropolitan New York" (GRB 16), more appropriately concedes that it only contacted those "which it had reason to believe" were selling dental products in Metropolitan New York (GRB 15). The facts establish that other dental dealers are located in Metropolitan New York which were not included. Their existence in the market is made clear by the Bureau of Census survey which lists 118 dental dealer establishments in the New York area (JA 313a), far more than the government survey identified.

5. *New Dental Dealer Entrants.* Healthco has demonstrated that within the last three years at least 10 dental dealers have entered the Metropolitan New York market selling dental equipment. (JA 859a-JA 860a). This fact alone not only demonstrates the incomplete picture which the government has presented with respect to actual competition in the sale of dental equipment, but also demonstrates the competitive vitality of the dental equipment market in the New York area. It is also, of course, reasonable to conclude that, if new dental dealers are entering the dental

equipment sales market within Metropolitan New York, new dental dealers outside Metropolitan New York, but selling into Metropolitan New York, are entering the dental equipment market.

A further indication of competitive vitality in the sale of dental equipment is reflected by the fact that several of the new entrants listed in the Kalik Affidavit (JA 859a-JA 860a) represent dental dealers who are expanding into the sale of dental equipment. Approximately half of the dental dealers surveyed by the government did not, in the past, sell dental equipment. (JA 800a) Consequently, it appears reasonable to conclude that there is a trend toward dental dealers entering into and expanding into the sale of dental equipment in the Metropolitan New York area. The many new manufacturers of dental equipment (see paragraph 2 above) can only accelerate that trend.

6. *Mail Order Dealers Within and Outside of Metropolitan New York.* The government made only perfunctory efforts to identify and analyze the extent of mail order dealer competition in the sale of dental equipment. (JA 325a). Trial testimony uncovered at least 23 sellers, consisting mainly of mail order sellers, which the government did not survey. (JA 111a-JA 124a). The Court virtually ignored such sales. This exclusion is particularly troublesome since the Court clearly recognized that:

> "The impact of the mail order houses is of increasing significance in the dental product industry." (JA 796a).

Although the Court below stated that it believed the impact was "largely" in the sundries area and that mail order sales were not "a significant factor" in the dental equipment area, the Court did recognize that "some items of equipment are sold by mail order houses." (JA 795a). In light of the growing importance of mail order dealers and the broad

geographic area in which they sell, it was improper to define the dental equipment market by excluding these suppliers. This is particularly true in light of the strong price competition which such sellers provide. (JA 795a, JA 810a-JA 811a).

Finally, the government's analysis makes no provision for the substantial growth of mail order dealers and the entry of new mail order dealers into the dental equipment market. Even within the Metropolitan New York area, Healthco identified six mail order companies which have increased their equipment sales and have expanded the scope of the equipment lines which they offer. (JA 860a-JA 861a).

* * *

Healthco recognizes that no one of the above categories of excluded dental equipment suppliers may account for a major percentage of total dental equipment sales to dentists. Nevertheless, in the aggregate, these six categories of sellers represent a substantial and growing competitive force in the sale of dental equipment, and demonstrate the total inadequacy of the government's narrow, distorted analysis of competition.* Each of these six categories of suppliers sells precisely the same equipment in competition with local dental dealers included in the government survey. These facts and the competitive presence of these sellers cannot be ignored.

As the government concedes, if the manufacturers of dental equipment who were surveyed are included in the market, the government's figures would produce a total market share for Healthco *20% smaller* than the government's estimate based on its partial survey. The resulting

* In addition, the mere fact that a category of sales *may* be relatively small is no basis to exclude those sales from the market. Such exclusion has been found to be a basis of reversible error. *International Telephone & Telegraph Corp.* v. *General Telephone & Electronics Corp., supra,* at 66,151-152.

market share is close to the market share which the government produced for sundries, the major submarket in which the District Court found no violation. It is safe to assume that the proper inclusion of the other six categories, or even a portion of the dental equipment sales of the other categories (which were either not surveyed by the government or partially surveyed and then ignored), would similarly produce, in the aggregate, a further substantial reduction in Healthco's market share.

Unfortunately, the government started with its own conclusion—that only the sales of the local dealers it surveyed constituted the market—and consequently these additional relevant sales figures are not available. The government must not be relieved of its burden of proof and permitted to partially measure the market, ignoring competitive realities, and then simply dismiss the balance of the competitors in the market by asserting that the ignored areas of competition are insignificant. A 20% decrease in market share from these sources alone is hardly insignificant.

Several additional factors indicate that the categories of excluded suppliers represent significant competition in the sale of dental equipment.

First. Most of the six categories of excluded sellers represent substantial *new* competition in the dental equipment market. The existence of this new and growing competition directly contradicts the District Court's belief that there has been no significant entry into the dental equipment market, that more suppliers are leaving the market than entering the market, or that concentration in the market is increasing. This new competition is summarized below:

> (a) *Manufacturers.* Healthco has identified more than 60 new dental equipment manufacturers which have entered the market since 1969 (p. 8, *supra*). These manufacturers represent a growing number of alternate sources of supply to dentists (as well as

institutions, dental labs and governmental agencies). They also represent an ever increasing range of alternate sources of supply to dental dealers in the market, and entering the market.

(b) *Dental Dealers.* Healthco has also indentified at least 10 local dental dealers who have entered the market by opening new businesses selling dental equipment, or who have entered the market by expanding their sales to include dental equipment. (JA862a). This new entry is particularly significant, because it reflects the judgment of informed dental dealers in the market that competitive opportunities exist in the sale of dental equipment.

(c) *Mail Order Dealers.* The Court recognized that significant expansion has taken place in terms of the number of mail order dealers in the market. (JA810a). The Court recognized that mail order dealers do sell some equipment. (JA795a, JA812a) Consequently, it is unreasonable to exclude such sales from consideration.

Second. The government's efforts to exclude substantial categories of manufacturer and mail order dealer competitors is based largely on the contention that such suppliers do not provide installation or after-sale service to dentists. This generalization is based on the apparent contention that a new dentist, graduating from school and initially setting up his practice, apparently needs the local service of a dental dealer. However, such sales represent no more than approximately 30% of dental equipment sales to dentists. (JA 862a). As to the 70% of sales to established dentists, several factors demonstrate that manufacturers and mail order dealers are realistic sources of supply to dentists. First, installation and service of dental equipment can be obtained from sources other than a local dental dealer. The District Court specifically recognized that:

> ". . . installation and repair services are available from independent companies specializing in such services." (JA 797a).

In addition, with the possible exception of dental chairs and some forms of dental units, installation service is not a significant requirement in purchasing dental equipment. Much dental equipment requires little or no "'installation." Moreover, established dentists are more experienced and knowledgeable and, therefore, more capable of making purchasing decisions, and arranging for installation and service, without the aid of a local dental dealer. These factors, in addition to the fact that dentists *do* buy equipment from manufacturers and mail order dealers, clearly demonstrate that manufacturers and mail order dealers must be considered competitors in selling to dentists.

Third. The increasing number of suppliers of dental equipment not only among manufacturers and mail order dealers but also among dental dealers, indicates that the market is becoming more and more fragmented. It has never been clear how a local geographic market with as many as 100 or more local dealers, depending on whose figures are used, and numerous manufacturers and mail order dealers can be described as "concentrated." Whatever the situation may have been in the late 1960's or in 1970, the dental equipment market has changed substantially since then. The Court recognized this in connection with the sale of dental sundries and found no violation (JA 823a-JA 824a); the same condition exists with respect to dental equipment. Although the Court below noted that prior to the acquisition, the number of dental dealers had decreased from 38 to 33 (JA 822a), this condition has dramatically reversed. Today there are at least 43 dental dealers selling dental equipment to dentists in the Metropolitan New York area (JA 859a-JA 860a), as well as an ever increasing number of manufacturers and mail order dealers.

Much of the evidence which the government and District Court ignored represented new competitive entry into the

dental equipment market. The advent of mail order dealer competition and the growth of dental equipment manufacturers represent a new competitive presence in the sale of dental equipment. The exclusion of these competitive sales from the market ignores the obligation that "a merger had to be viewed, in the context of its particular industry" because "only a further examination of the particular market—its structure, history and probable future—can provide the appropriate setting for judging the probable anticompetitive effect of the merger." *Brown Shoe* v. *United States*, 370 U.S. 294, 322 (1912), cited with approval in *United States* v. *General Dynamics Corp.*, 415 U.S. 486, 498 (1974). The Court below rejected this approach, and ignored the requirement, set forth in *General Dynamics*, that changed conditions in an industry must be given full consideration. As to this requirement, the Court below stated that the changes in the dental equipment industry were "in the future" and "speculative", whereas the changes in *General Dynamics* "had already taken place." (JA 826a). This is in error. The new entry in the market by manufacturers, mail order dealers and local dental dealers "has already taken place", as set forth above. Just as the government ignored the current state of the market in *General Dynamics* under a "traditional analysis" of past market shares, the government and the District Court have ignored the new entry and changing competitive conditions in the dental equipment market.*

* The government argues that these facts are "post-acquisition evidence" having little probative value. However, the Supreme Court in *General Dynamics, supra*, relied heavily on post acquisition evidence of developments in the market (as opposed to the conduct of the merged companies). The Court found such evidence highly probative because it "could not reflect a positive decision on the part of the merged companies to deliberately, but temporarily refrain from anticompetitive actions." (*Id.* at 506).

The proper inclusion of these six categories of dental equipment competitors, in addition to the inclusion of the manufacturers' sales which the government has set forth in its Reply Brief, renders the government's market share analysis totally invalid. As a result, the Court below had no basis for finding a Section 7 violation in the dental equipment market.

II.

The Variance Between the Government's and the Industry's Estimates of the Size of the Market Can Only Be Explained by the Improper Exclusion of the Categories of Competitors Described Above.

Substantial volumes of evidence have been introduced by both parties with respect to the size of the relevant market. The government, for its part, surveyed certain local dental dealers, and produced a total market of approximately $32 million. Healthco did not have the burden of proof in establishing the size of the relevant market. However, Healthco has submitted data from industry sources, government sources, and industry experts to demonstrate that the government's approach vastly understates the size of that market.

Significantly, every one of the sources of industry and government data, and each of the industry experts, confirmed that the total market is much larger than the government's. In addition, each of those sources, using independent and differing methods of computation, estimates a market roughly consistent with one another. In short, all roads lead to the same result—except the government's:

> (a) The Bureau of Census data indicates that the market is nearly twice as large as that in the government survey (approximately $55 million). (Brief for Healthco, Inc. 48-49, hereinafter "HB ").

(b) David Ellis, statistician for the American Dental Trade Association, using industry data, concluded that the total market was approximately twice the size of the government's figures (approximately $60 million), and the government's expert, Dr. Schwartzman, testified that he had no reason to believe Mr. Ellis was incorrect. (HB 49-50).

(c) Dr. Gould, an economic consultant, concluded that the market was nearly twice as large as the government's estimate (approximately $58 million). (HB 50-51).

(d) A periodic dental industry survey by a trade journal, Proofs Magazine, produced a larger sales figure for dental sundries sales than the government's figures for total dental product sales. This means that the total market, based on the Proofs survey would, again, be approximately twice as large as the government's figures (approximately $58 million). (HB 51-52).

Thus, each of four different data sources rebut the validity of the government's figures, and are basically consistent with one another ($55, $60, $58 and $58 million). In each instance these data sources, all of which are normal industry data, and none of which was created for this litigation, indicate that the government's figures represent only about one-half of the total relevant market. It is recognized that the government's methodology was inadequate, and the responses received were inaccurate. (HB 43-46).* However, such a vast difference between the government's figures, and four different evaluations based on government and industry data can lead to no other conclusion than the fact that the government started with the wrong universe of sellers. It surveyed only certain local

* An example of the inaccuracy of the government survey is the fact that one respondent testified that his answer to the government survey as to his sales ($225,000) had been "a guess". (JA 684a). His sales actually were in excess of $600,000. (JA 685a).

dental dealers and produced a "market" which did not reflect the commercial realities of competition. This is not a question of inadmissibility of survey evidence, but rather a question of the failure to measure the full scope of the relevant market by a survey which ignores substantial categories of competitors. This failure is particularly telling, where all indications from government and industry sources, which were available to the government, conclude that the market was much larger.

The government survey so understates the market, and misinterprets the nature of competition that it is impossible to determine what the actual relevant market shares are. Two things are certain, however. One, the government improperly excluded vast categories of competitors; two, their proper inclusion would substantially lower Healthco's market share. The inclusion of manufacturers surveyed, reflected in the government's Reply Brief, would lower Healthco's market share close to the market share found for dental sundries—where no violation existed; the proper inclusion of the other six categories of dental equipment competitors would be likely to lower Healthco's market share far below that found in sundries.

These conclusions, as well as the fact that the dental equipment market exhibits the same pro-competitive characteristics as the sundries market (discussed below in Point III), require that the finding of a violation in the dental equipment market be reversed.

III.

Legal Analysis of the Dental Equipment Market, Using the Court's Criteria Applied to the Sundries Market, Shows No Likelihood of Injury to Competition.

The Court below properly found no violation in the dental sundries market:

> "In the dental sundries submarket, the share controlled by Healthco, the increasing trend of mail order houses as a competitive force in this market, and other evidence satisfy this Court that Section 7 has not been violated by the four challenged acquisitions" (JA 824a).

However, the Court believed that the market share controlled by Healthco in dental equipment was substantially larger than in dental sundries—as a result of the government's improper market analysis, discussed above. Had the Court properly recognized the broader scope of competition, and had the government submitted market share data reflecting that competition, a market share figure much lower than the market share for sundries would have been likely.

In addition, if the Court below had recognized the need to include the other categories of dental equipment sellers, the Court undoubtedly would have reached the same conclusion with respect to the inadequate government survey as it did in the sundries market:

> ". . . there are believed to be omissions from the total sales of sundries and there can be no acceptance of the statistical exhibits as showing accurately Healthco's share of the dental sundries submarket in 1969 and 1970. The share is speculative." (JA 823a).

The Court below points to several other factors which it believed distinguishes the dental equipment and sundries

submarkets. Here again, however, these distinctions are not valid. While the Court found increasing competitive forces in sundries sales, it failed to recognize the same type of increasing competitive entry into the dental equipment market.

Thus, the Court stated that prior to the challenged acquisitions the number of dental equipment dealers dropped from 38 to 33. However, as noted above, at least 10 dental dealers, 60 manufacturers, and at least 6 mail order dealers in the New York area alone have *entered* the dental equipment market or expanded their dental equipment sales since 1968. Surely, such a significant entry into the dental equipment market at least parallels the "increasing trend of mail order houses as a competitive force in [the sundries] market". (JA 824a).

The Court also believed that entry barriers in dental sundries did not appear to be great, but that there were economic barriers to entry in the sale of dental equipment. One of the reasons for the Court's conclusion, the lack of entry of new sellers, has, of course, been refuted above.*

The Court also believed that equipment lines were not readily available from manufacturers to dental dealers seeking to enter the business, or to add equipment lines, thereby creating entry barriers. Here again, the entry of a large number of dental equipment manufacturers refutes this argument. In addition, the fact exists that as many as 10 dental dealers have entered the dental equipment market since 1968. Obviously, they have been able to obtain dental equipment lines and their significant number refutes any argument that equipment lines cannot be obtained by dental dealers.

---

* The Court did properly recognize that "Entry into the equipment submarket is not foreclosed by patents or by technological reasons." (JA 821a-JA 822a). The lack of such barriers is underscored by the entry of more than 60 dental equipment manufacturers since 1968.

The Court further noted that, unlike sundries, it is not economically feasible for a dental dealer to sell equipment only. This is not supported by the record, and is also not relevant. What is important is whether a dental dealer can obtain sundries lines to sell. As the Court found, dental sundries suppliers are readily available, and thus there is nothing to prevent a dental equipment dealer from selling sundries along with dental equipment.

The Court further believed that capital requirements for entry into the sale of dental equipment were high, stating that in excess of $100,000 is required for a dental dealer who wishes to offer full equipment and sundries lines. Although subjective evaluations may vary as to whether this figure is a high capital requirement, the fact remains that dental dealers have been entering the dental equipment market in Metropolitan New York. (JA 862a).

Healthco believes that any analysis of the effects on competition of an acquisition must be based upon what actually occurs, or is likely to occur, in the market. The evidence demonstrates that the competitive characteristics of the dental equipment market are substantially similar to those of the dental sundries market, where no violation was found. These similar characteristics demonstrate that the relative ease of entry in dental sundries also applies to the sale of dental equipment. In addition, there is clear and unrefuted evidence that substantial new entry in the sale of dental equipment has in fact taken place and has been increasing over the last seven years. Finally, such new entry, and particularly the new entry and competitive impact from mail order dealers, provides increased price competition (JA 795a, JA 810a-JA 811a).

The government, in its Reply Brief, repeatedly attempts to compare Healthco's position in the dental equipment market with the share of other markets, including groceries, coal, banking, etc. However, the Supreme Court has

concluded that such a "numbers game" involving different industries is not appropriate because a merger must be functionally viewed, in the context of its particular industry. *Brown Shoe Co.* v. *United States*, 370 U.S. 294, 322 n.38 (1962). Thus, the functional characteristics of the dental equipment market are most properly compared with the characteristics of the dental sundries market, as has been done above. The result shows not only similar functional characteristics, but also that the market share is undoubtedly smaller than the market share in sundries, where no violation existed.

This fact, and the government's failure to introduce any evidence of control over prices or anticompetitive market power, lead to the conclusion that there is no basis to find a violation in the dental equipment market.

IV

The Evidence Demonstrates That No Divestiture is Appropriate in This Proceeding and That the Court's Discretion in Fashioning the Order, If Erroneous, Favored the Government.

Notwithstanding the substantial problems which the government faces in attempting to salvage the one submarket in which a violation was found, the government still contends that the relief granted was inadequate. Based on the evidence set forth above, it is impossible to see how the government can contend that "all doubts as to the remedy" were not resolved in favor of the government.

Healthco contends that the strong competitive vitality in the dental equipment market in the New York area based upon new entry, new availability of sources of supply, and expanding competition from manufacturers and mail order dealers can only lead to the conclusion that no divestiture

is required in this proceeding. Divestiture is "an extremely harsh remedy and should be decreed as to property obtained by an acquisition only when necessary to the restoration of the competitive situation altered by the acquisition." *Reynolds Metals Co.* v. *FTC*, 309 F.2d 223, 231 (D.C. Cir. 1962). In this proceeding, the factors described above support a conclusion that the current competitive situation is not merely as competitive as prior to the acquisitions, but more intensely competitive.

For these reasons, Healthco contends that the divestiture order is not appropriate or necessary.

If, however, the Court believes that some form of divestiture is necessary, the proposed method of divestiture ordered by the Court below is more than adequate. In a very real sense, the Order entered requires more than total divestiture. Healthco must not only divest itself of the dental equipment business involved in the challenged acquisitions, but it also must divest itself of dental equipment assets which it held prior to the challenged acquisitions.

The Final Order reflects a careful review of the Court's opinion to ensure that the divested entity will have all necessary assets successfully to establish itself as a viable competitor. All of Healthco's dental equipment specialty salesmen will be given to the new company; the new company will have a well-equipped centrally located headquarters with all necessary service and repair personnel; the new company will have access to suppliers of dental equipment; Healthco will provide assistance to insure that these manufacturer contacts are retained and developed; and the new company will have a ready-made portfolio of customers, whose relationships with the dental equipment specialty salesmen transferred to the new company will permit the new company successfully to operate its dental equipment supply business.

The government contends that the new company will not have sundries lines and therefore cannot succeed. How-

ever, as the Court recognized, there is no evidence that any economic or other barriers exist to prevent dental dealers from obtaining sundries lines.

The government also contends that, since Healthco made four acquisitions, four companies should be divested. This argument is totally inconsistent with the government's concern with the creation of a viable entity. As noted, two of the acquired companies were in financially weak condition (HB 32, 36-37). To reconstruct their position prior to the acquisitions would provide no competitive benefit. The Court below apparently recognized this and has fashioned an Order which will add viable competition to the market. In light of the increased number of competitors selling dental equipment, to require more than this would be unnecessary and punitive. This is particularly true because current competitive conditions suggest that *any* divestiture is of dubious necessity to "restore" competition.*

Thus, not only are the government's concerns ill-founded, but the divestiture Order provides more than adequate remedial relief. In fact, the competitive structure of the dental equipment market is such that it is difficult to see why any divestiture is necessary.

V

Conclusion

Healthco respectfully requests that this Court reverse the finding of a violation in the dental equipment market

* As to the government's concern that Healthco could retain equipment inventories, and that the Order does not give the government or the Court the right to approve the purchaser of the divested assets, Healthco would be more than willing to sell its equipment inventories to the purchaser, and to give both the Court and the government a right to approve that purchaser.

because of the failure of the government to properly analyze the scope of competition in the market; because of the grossly inaccurate and understated market share data submitted by the government; and because of the substantially increased competition which has taken place in the dental equipment market.

Healthco also respectfully requests that, regardless of the Court's conclusion as to a violation of Section 7 in the dental equipment market, this Court vacate the divestiture order as being unnecessary and inappropriate because of the current competitive state of the market.

Respectfully submitted,

EDWARD L. FOOTE
THOMAS WM. BIANCHI
Attorneys
WINSTON & STRAWN
Suite 5000
One First National Plaza
Chicago, Illinois 60603

Of Counsel:

IRA M. MILLSTEIN
PETER D. STANDISH
Attorneys,
WEIL, GOTSHAL & MANGES
767 Fifth Avenue
New York, New York 10022

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT
----------x

UNITED STATES OF AMERICA,

Plaintiff-Appellant,

-against- No. 75-6011

HEALTHCO, INC.

Defendant-Appellee.

----------x

On Cross-Appeals From the United Stat
District Court for the Southern District

CERTIFICATE OF SERVICE

I, Peter D. Standish, hereby certify that I have on this 7th day of October, 1975, served by mail a copy of the Reply Brief of Defendant/Appellee, Healthco, Inc., in the above reference proceeding upon the following persons:

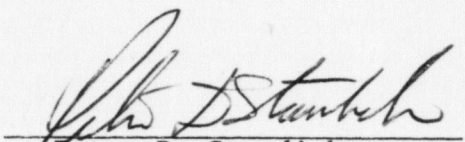
Thomas E, Kauper, Esq.
Assistant Attorney General
Department of Justice
Antitrust Division
Washington, D.C. 20530

Carl D. Lawson, Esq.
Department of Justice
Antitrust Division
Washington, D.C. 20530

John J. Powers III, Esq.
Department of Justice
Antitrust Division
Washington, D.C. 20530

Melvin Lublinski, Esq.
Department of Justice
Antitrust Division
26 Federal Plaza
New York, New York 10007

John Sirignano, Jr., Esq.
Department of Justice
Antitrust Division
26 Federal Plaza
New York, New York 10007



Peter D. Standish
Attorney
Weil, Gotshal & Manges
767 Fifth Avenue
New York, New York 10022
Attorneys for Defendant-Appellee
Healthco, Inc.

NOTICE OF ENTRY

Sir :—Please take notice that the within is a (certified) true copy of a
duly entered in the office of the clerk of the within named court on 19

Dated,

Yours, etc.

WEIL, GOTSHAL & MANGES

Attorneys for

Office and Post Office Address

767 FIFTH AVENUE

Borough of Manhattan New York, N.Y. 10022

To

Attorney for

NOTICE OF SETTLEMENT

Sir :—Please take notice that

of which the within is a true copy will be presented for settlement to the Hon.

one of the judges of the within named Court, at

on the day of 19

at M.

Dated,

Yours, etc.

WEIL, GOTSHAL & MANGES

Attorneys for

Office and Post Office Address

767 FIFTH AVENUE

Borough of Manhattan New York, N.Y. 10022

To

Attorney for

Index No. 75-6011 *Year* 1975

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

UNITED STATES OF AMERICA,

Plaintiff-Appellant,

-against-

HEALTHCO, INC.

Defendant-Appellee

REPLY BRIEF OF HEALTHCO, INC.

WEIL, GOTSHAL & MANGES

Attorneys for Healthco, Inc.

Office and Post Office Address, Telephone

767 FIFTH AVENUE

Borough of Manhattan New York, N.Y. 10022

PLAZA 8-7800

To

Attorney for

Service of a certified copy of the within
is hereby admitted.

Dated,

Attorney for